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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation	)	MM Docket No. 92-266

REPLY COMMENTS OF VIACOM INTERNATIONAL INC.

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Viacom International Inc. ("Viacom"), by its attorneys, hereby submits its reply comments on the Commission's Third Notice of Proposed Rulemaking in its rate regulation proceeding, which seeks to refine several critical elements of the Commission's regulatory framework that threaten to eliminate existing marketplace incentives for increased investment in cable service and programming.[1] Viacom submits that the record in this proceeding amply supports the Commission's proposals, tailored in the manner described below, to allow cable operators to recover their investment in continued improvements in the service and program offerings they provide to the American viewing public.

INTRODUCTION AND SUMMARY

Viacom's initial comments urged the Commission to adopt rules that would preserve the vibrant cable programming

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[1] First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking, MM Docket No. 92-266 (released August 27, 1993) ("Reconsideration Order" or "Third Notice").

marketplace that existed prior to rate regulation.[2] Viacom sought to ensure, in particular, that the Commission provide cable operators a ready means to recover the full range of costs incurred in upgrading the quality and diversity of programming available to cable subscribers -- not only additional programming costs, but also the system upgrade costs that are a prerequisite for most systems to offer additional program services.

A wide range of commenters essentially concur with the Commission's proposal to adjust an operator's benchmark at least to cover all programming costs incurred when adding program services. The only material disagreement concerns whether the FCC's proposal would achieve its objective. The Massachusetts Community Antenna Television Commission ("MCATC") and a number of other parties joined Viacom in questioning whether the Commission's preferred approach would, in fact, provide sufficient means and incentives for operators to add channels.[3]

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[2] See Comments of Viacom in MM Docket 92-266 (filed September 30, 1993). See also Comments of The Disney Channel ("Disney") and Comments of Discovery Communications, Inc. ("Discovery") (both supporting recovery of programming costs, including a reasonable mark-up).

[3] See Comments of MCATC at 2-3; see also Comments of New York State Commission on Cable Television at 2-3; Comments of GTE Service Corporation at 3-8; Comments of Discovery at 5-8; and Comments of Disney at 2-8.

While the debate over programming costs has evolved into a discussion of the best means of -- rather than the need for -- recovery of such costs, some commenters remain reluctant to acknowledge the need for recovery of the associated capital costs of system improvements. Absent sufficient channel capacity, however, viewers will be denied the breadth and quality of programming that the Cable Television Consumer Protection and Competition Act of 1992 and the Commission envision.[4] As discussed in the following section, Viacom submits that the Commission's rule according external treatment to the costs of complying with franchise requirements should apply perforce to costs incurred in constructing franchise-required upgrades. This external treatment should be achieved through application of the Commission's streamlined cost-of-service measures, which should be made applicable to voluntary upgrades as well.

Among the range of proposals for the coordination of federal and local rate regulation, the record evinces broad support for the use of a regulatory methodology that would prevent "gaming", but also avoid duplicative determinations at the FCC and the local forum. Specifically, many operators voiced support for an approach, like the one proposed by Viacom, that would allow operators to cost-justify rates for

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[4] See Pub. L. No. 102-385, 106 Stat. 1460 (1992) (the "Act" or "1992 Cable Act").

expanded tier service without also filing a needless cost showing before local authorities. Viacom also recommends that the Commission take a lead role in the coordination of these cost showings that directly implicate important federal interests in infrastructure development.

I. CONTINUED INVESTMENT IN IMPROVING THE QUALITY AND BREADTH OF CABLE SERVICE AND PROGRAM OFFERINGS WOULD SUFFER IF THE COMMISSION WERE TO ABDICATE ITS STATUTORY DUTY TO ENSURE THE RECOVERY OF SYSTEM UPGRADE COSTS

Viacom recommends that the FCC adopt rules permitting operators to recover the costs incurred in upgrading their systems, whether the upgrade is required by the franchising authority or voluntarily undertaken by the operator. Distinguishing between upgrades on this basis would threaten to delay the construction of system improvements to the detriment of cable subscribers and the federal interest in an advanced telecommunications infrastructure. Viacom advocates a complementary, streamlined approach to recovery of these costs that preserves operators' incentives to invest in improved system capacity and technical capabilities.

The 1992 Cable Act clearly calls for rate regulations that allow operators to recover their costs, specifically including both the costs of system upgrades and the costs of

complying with franchise requirements.[5] Moreover, franchise-required upgrade costs logically should be treated no differently than other franchise requirements, for which the FCC's rules appropriately provide recovery on an external basis. Indeed, the Commission has already determined that service and technical requirements specifically required by a franchising authority should be accorded external

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[5] See 1992 Cable Act at § 2(b)(3) (policy of 1992 Cable Act to expand the capacity of cable systems); 47 U.S.C. § 543(b)(2)(C)(vi) (FCC rate regulations shall take into account operators' costs of complying with franchise requirements); and Reconsideration Order at ¶ 102 (increases in the costs of complying with franchise requirements are eligible for external treatment).

The comments of Austin, Texas, et al. ("Austin") strain credulity in suggesting (at 3) that an earlier Viacom submission can be read as demonstrating that benchmark rates already allow operators to fully recover the cost of upgrades. Austin cites to the study submitted with Viacom's Petition for Reconsideration and Clarification in Docket 92-266 (filed June 21, 1993), which noted that the overbuild systems included in the benchmark rate survey -- which on average are newer and have greater channel capacity than other systems surveyed -- charge lower per-channel rates than other systems. Austin asserts on this basis that other cable operators' future costs in upgrading system capacity would be fully covered by the rates in effect for these overbuild systems as of September 1, 1992. It remains unclear whether these rates were fully compensatory and sustainable even for the overbuild systems surveyed. It is beyond doubt, however, that the average 1992 "snapshot" rates for these systems simply cannot be assumed to produce compensatory rates throughout an industry undergoing a new wave of progressive upgrades to expand service and prepare for new competition. Moreover, the very study that Austin cites with approval demonstrates that the existing benchmarks fail even to accurately measure the average competitive rates they purport to represent.

treatment.[6] As a matter of policy, furthermore, the Commission correctly observes that local authorities are in a position to weigh the impact of upgrade costs on subscriber rates at the time upgrades are required.[7]

While there thus exist distinct legal and policy grounds for external treatment of franchise-required upgrades, the Commission should also ensure an equally viable means for recovery of upgrades that are undertaken voluntarily. Indeed, a number of factors compel adoption of a similar approach to the recovery of upgrade costs, whether required in a franchise agreement or initiated by the operator. Several commenters rightly point out that a significant difference in the ability to recover the costs of franchise-required upgrades, as opposed to voluntary upgrades, could lead to contentious disputes as to whether a certain upgrade cost is indeed "required by the franchise."[8] These commenters wrongly conclude, however, that consistency calls for subjecting both classes of upgrades to the broad discretion of local franchising authorities. Rather,

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[6] Reconsideration Order at ¶ 102 & n.176.

[7] See id. at ¶ 97.

[8] See, e.g., Comments of National Association of Telecommunications Officers and Advisors, et al. ("NATOA") at 4-8. Such a possibility is made more likely given that in certain cases multiple franchise authorities regulate the same system. Indeed, Viacom operates a system in the State of Washington that is potentially subject to regulation by 48 different local authorities.

continued improvement of the channel capacity, programming diversity, and signal quality of the cable service offered to the American public requires that operators have a certain and efficient means for recovering the costs of upgrades in either case -- required or voluntary. Viacom therefore submits that franchise-required upgrade costs should be calculated by using the streamlined cost-of-service standards proposed by the Commission and then passed through as an external cost; the costs of a voluntary upgrade similarly should be recoverable through a streamlined cost-of-service showing.[9]

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[9] See Notice of Proposed Rulemaking, MM Docket No. 93-215, FCC 93-353 (released July 16, 1993) at ¶ 75. Viacom is confident that these costs can be readily determined through the use of this streamlined cost-of-service proposal set forth by the Commission and advocated by Viacom and a number of other commenters. See, e.g., Viacom Petition for Reconsideration in MM Docket No. 92-266, supra.

Austin nonetheless suggests that determining the amount of franchise-required upgrade costs that may be passed through -- which it argues would require determining the original cost of the system adjusted for inflation -- would actually be more complex than a full cost-of-service showing. See Austin at 4-7. This assertion is wrong for several reasons. For one, cost-of-service showings for upgrades would not need to account for inflation as an independent factor because inflation would already be offset by the fact that operators recover their costs over an extended period of time. The same would be true if the FCC adopts Viacom's proposal for trended original cost ("TOC"), which already considers and deducts inflation from the rate calculus. See Comments of Viacom in MM Docket No 93-215 (explaining the TOC methodology for determining the value of cable assets on a going forward basis).

Furthermore, uniform treatment of costs is especially appropriate in matters relating to cable system infrastructure. Indeed, longstanding federal policy has recognized the overriding national interest in the development of advanced telecommunications infrastructure. This vital federal interest could be effectively thwarted by a patchwork of inconsistent local determinations.[10] The local role should be limited to examining the legitimacy of costs incurred in upgrading a system.

II. THE COMMISSION SHOULD ENSURE AN ORDERLY, COORDINATED COST-OF-SERVICE MECHANISM BY ESTABLISHING UNIFORM FEDERAL GUIDELINES AND AVOIDING UNNECESSARY LOCAL SHOWINGS

Viacom urges the Commission to take an active role in ensuring that the local administration of its cost-of-service rate regulation rules is consistent with federal determinations. Viacom thus recommends, as a starting point, that the Commission adopt a streamlined cost-of-service approach such as that proposed by Viacom in Docket 93-215. In addition, the Commission should coordinate federal and

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[10] The contrary comments of several localities seem to be based on the unfounded assumption that cable operators would "goldplate" and charge rates without regard to subscriber dissent. It has never been seriously contended, however, that demand for cable service is completely inelastic. It would be the height of folly for a cable operator to upgrade its system so as to enhance its competitive posture, but in so doing readily allow alternative distributors to underprice it.

local cost showings to the greatest extent possible, in particular by allowing operators to justify expanded tier rates without also making a needlessly duplicative local showing as to benchmark-consistent basic rates.[11]

Many commenters, including both operators and regulators, voiced support for a strong FCC lead in the coordination of federal and local regulation of cable rates.[12] Viacom concurs that the FCC, at the very least, should adopt uniform guidelines governing all significant cost-of-service standards. Indeed, if the cost-of-service process is to be rational and predictable, the FCC must establish the ground rules for all such showings.

In its cost-of-service comments, Viacom suggested a comprehensive set of proposals through which the Commission could streamline its cost-of-service rules.[13] Viacom urged the Commission to adopt, among others, the following specific

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[11] Viacom urges the Commission to reject the comments of parties who remain determined to erect threshold requirements or other limitations on the operators' fundamental right to seek cost-of-service showings. As numerous commenters have explained and the Commission itself has clearly recognized, the statutory and constitutional validity of its rate regulations depends in large part on the ready availability of a mechanism for ensuring a reasonable return on operators' investment in providing cable service. Anything less would threaten the ability of cable operators to provide subscribers the service they desire. See Power Comm'n v. Hope Gas Co., 320 U.S. 591, 603 (1944).

[12] See, e.g., MCATC at 6-8.

[13] See Comments of Viacom in MM Docket No. 93-215 (filed August 25, 1993) at 42-56.

measures: (1) a uniform, industry-wide rate of return; (2) the depreciation of cable assets in broad categories at the system level on a straight-line basis over their economic lives; (3) simple cost allocation and cost accounting requirements, including the aggregation of most costs on a system-wide basis. These uniform standards would provide a complete, yet simplified approach to cost-of-service rate regulation that is fair to both operators and subscribers.

Given the Act's reliance on the Commission to establish the standards for cost-of-service showings, many commenters appropriately call for the consolidation at the FCC of at least those cost proceedings where duplication and inconsistency would otherwise likely occur.[14] One widely supported method to eliminate "gaming", while still ensuring federal coordination of cost showings, is the proposal advanced by Viacom and many other commenters: allow operators to file cost-of-service showings to justify expanded tier rates, without also filing a cost showing at the local level to justify basic rates consistent with

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[14] At a minimum, the Commission should adopt the approach advocated by MCATA, which would allow local authorities to opt out of requiring cost justification for benchmark-consistent basic rates at the local level where an operator has made a cost showing before the FCC. See MCATC at 7.

benchmark regulation.[15] As Viacom explained in its comments, such a proposal would allay fears of "gaming" by requiring operators, who already must submit cost data allocated across all tiers in justifying expanded tier rates, to demonstrate further that basic rates do not exceed the presumptively reasonable levels permitted by the benchmark approach.

Federal coordination of cost showings could be further facilitated through a number of practices commenters have proposed, such as removal of contemporaneous local cost-of-service showings at the local level, making local authorities a party to the federal proceeding, providing for forwarding of records between the FCC and local authorities, and by providing that federal findings are entitled to substantial deference at the local level.

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[15] See, e.g., Comments of Cablevision Industries Corp., et al. at 11-14; Comments of National Cable Television Association at 16-17; and Comments of KBLCOM, Inc., et al. at 6-7.

CONCLUSION

For the foregoing reasons, Viacom respectfully urges the Commission to adopt the proposals advocated herein. By enacting uniform rules that permit operators to recover expeditiously the costs incurred in system improvements and by coordinating those rules primarily at the federal level, the Commission will ensure that the viewing public continues to receive the benefits of improved cable service and diverse program offerings.

Respectfully submitted,

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